Monetary and Financial Developments

HIGHLIGHTS

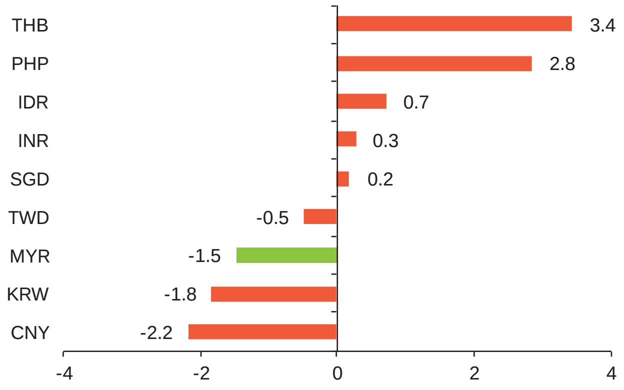
- **The ringgit depreciated in the second quarter amid global and domestic uncertainties.**
- **The performance of domestic bond and equity markets were supported by sustained demand from domestic institutional investors.**

The performance of domestic financial markets were mixed during the second quarter

During the first two months of the quarter, domestic financial markets were affected by cautious investor sentiments amid the moderating global growth outlook and escalations in global trade tensions. Domestically, potential reviews on Malaysia's inclusion in the FTSE Russell World Government Bond Index (WGBI) also weighed down sentiments in the domestic bond market. As a result, non-resident portfolio outflows of RM5.1 billion led the ringgit to depreciate by 1.5% against the US dollar during the quarter. Despite the weak sentiments, domestic bond and equity markets remained supported by sustained demand from domestic institutional investors throughout the quarter.

Ringgit depreciated against the US dollar, driven by non-resident portfolio outflows

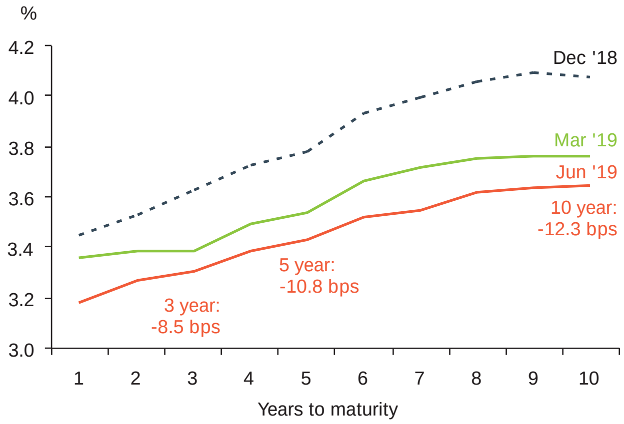
Chart 19: Performance of Regional Currencies Against the US Dollar (1 April - 28 June 2019)



Source: Bank Negara Malaysia

MGS yield curve shifted downwards during the second quarter

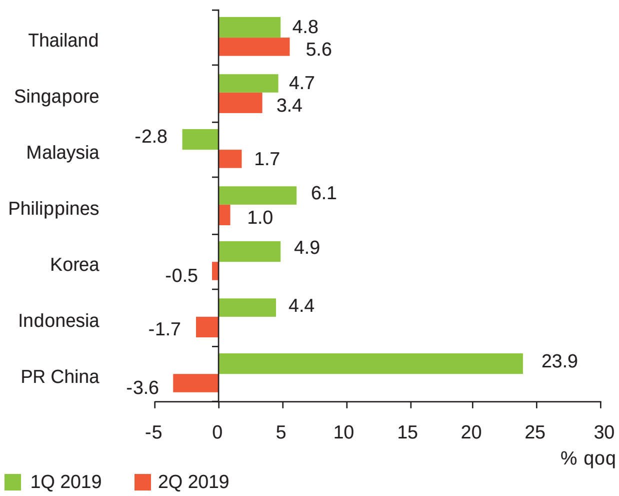
Chart 20: Trend in MGS Yields



Source: Bank Negara Malaysia

Domestic equity market performance improved during the quarter

Chart 21: Performance of Regional Equity Markets



Source: Bloomberg

Towards the end of the quarter, the performance of domestic bond and equity markets were lifted by a recovery in investor sentiments. In June, expectations of monetary policy easing by major central banks led to an improvement in global investor risk appetite, which spurred a recovery in non-resident portfolio inflows. As a result, the FBM KLCI increased by 1.7% in the second quarter to close at 1,672.1 points as at end-June (end-March 2019: 1,643.6 points) and the 3-year, 5-year and 10-year MGS yields declined by 8.5, 10.8 and 12.3 basis points, respectively.

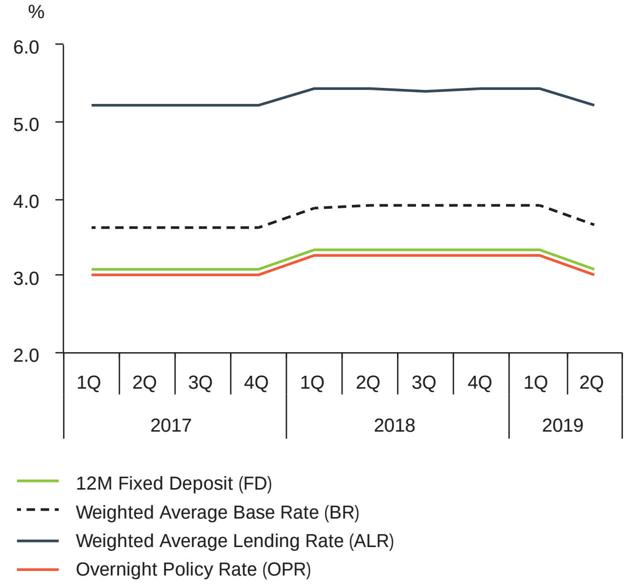
Interest rates decreased during the quarter given the reduction in the Overnight Policy Rate (OPR)

Following the reduction in the OPR on 7 May 2019, interest rates in the wholesale and retail markets trended lower. In the interbank market, strong and immediate pass-through was observed, with the 3-month KLIBOR decreasing by 23 basis points to 3.46% (1Q 2019: 3.69%). Similarly, nominal fixed deposit (FD) rates also decreased following the OPR adjustment. The decline ranged from 24 to 25 basis points across tenures of 1 to 12 months. Correspondingly, real FD rates decreased given the decline in nominal rates and higher inflation during the quarter.

For the retail segment, the transmission of OPR to base rate (BR) was also strong, with all banks revising their BRs downwards by 25 basis points to the current weighted average of 3.68% (1Q 2019: 3.92%). By end-quarter, the weighted average lending rate (ALR) on outstanding loans was also lower by 20 basis points at 5.23% (1Q 2019: 5.43%).

Interest rates decreased following the reduction in the OPR

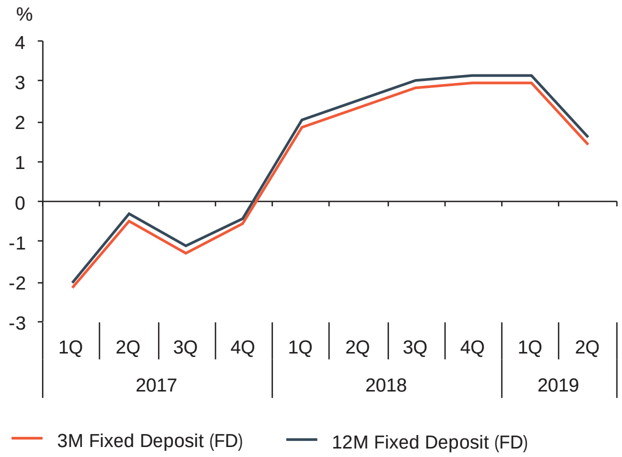
Chart 22: Fixed Deposit Rate, Base Rate and Average Lending Rate (at end-period)



Source: Bank Negara Malaysia

Real deposit rates declined

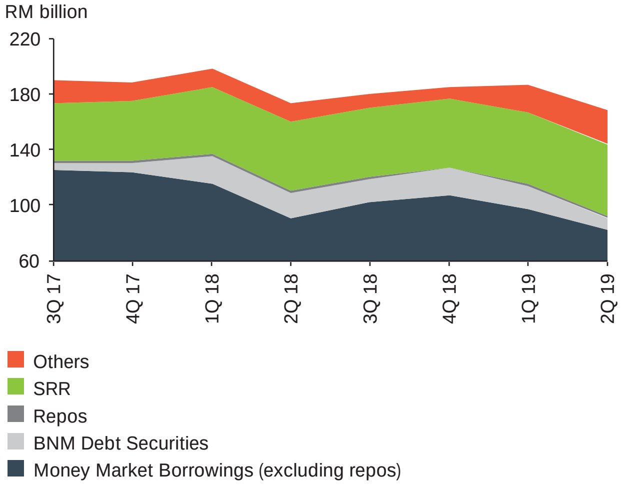
Chart 23: Real Fixed Deposit Rates by Maturity (at end-period)



Source: Bank Negara Malaysia

Outstanding surplus ringgit liquidity placed with the Bank declined

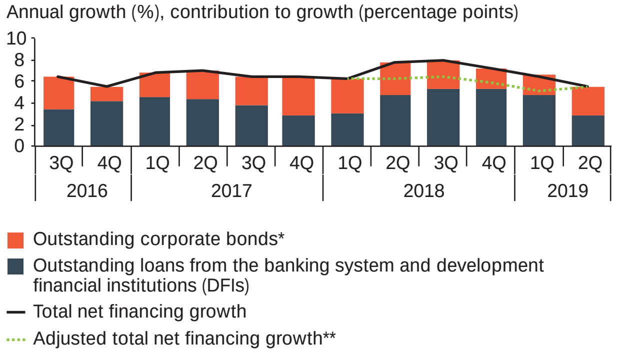
Chart 24: Outstanding Ringgit Liquidity Placed with Bank Negara Malaysia as at end-period



Source: Bank Negara Malaysia

Net financing continued to grow as outstanding loans and corporate bonds continued to expand

Chart 25: Contribution to Net Financing Growth



* Excludes issuances by Cagamas and non-residents
** Removing transitory impact for the period of 2Q 2018 to 1Q 2019, due to the inclusion of data for a newly licensed commercial bank (MBSB Bank Berhad) from April 2018

Source: Bank Negara Malaysia

Liquidity conditions remained sufficient to facilitate financial intermediation

The level of surplus liquidity placed with the Bank decreased, reflecting the net outflows during the quarter. Notwithstanding this, liquidity conditions remained sufficient in the banking system at both the system-wide and institutional levels, with most banks continuing to maintain surplus liquidity positions with the Bank.

Net financing continued to expand during the quarter

In the second quarter, net financing expanded by 5.6% on an annual basis (1Q 2019: 6.5%), driven by the continued expansion of outstanding corporate bonds[5] and loans[6]. Growth of outstanding corporate bonds increased to 10.6% during the quarter (1Q 2019: 7.1%), largely driven by a one-off issuance in the finance, insurance, real estate and business services sector. Outstanding total loans recorded a 3.9% growth on an annual basis (1Q 2019: 6.4%), with outstanding business loans expanding by 2.7% (1Q 2019: 4.4%), while outstanding household loans grew by 4.8% (1Q 2019: 7.5%). Apart from a low base effect for the first quarter of 2019 due to the inclusion of data for a newly licensed commercial bank from April 2018 onwards[7], the moderation in growth of outstanding total loans in the second quarter of 2019 reflected the high loan repayments, which outpaced disbursements.

For the business segment, a steady level of loans were disbursed to both SMEs and non-SMEs (total loans disbursed to businesses: RM197.2 billion, 1Q 2019: RM193.8 billion). Loans were mainly disbursed to the manufacturing; wholesale and retail trade, restaurants and hotels; and construction sectors, in line with the continued economic expansion in these sectors. Demand for financing among businesses showed some signs of improvement during the quarter as loan applications[8] increased (RM95.5 billion, 1Q 2019: RM77.4 billion). For the household segment, loans for residential property continued to be the primary driver of household loan expansion (contribution to growth: 3.8 percentage points), supported by sustained approval rates for housing loans.

5 Corporate bonds exclude issuances by Cagamas and non-residents.
6 Loans from the banking system and development financial institutions (DFIs).
7 Effective June 2019, data for April 2018 onwards were revised to include data from a newly licensed commercial bank (MBSB Bank Berhad). It was previously classified as a non-bank financial institution. The inclusion of the outstanding loan figures resulted in higher financing annual growth rates for a transitory period from 2Q 2018 to 1Q 2019 due to the lower base in preceding years.
8 Loan applications to the banking system only.